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Supreme Court of the United States

OCTOBER TERM, 1963

PEOPLE OF STATE OF CALIFORNIA, *et al.*, SOUTHERN CALIFORNIA GAS COMPANY *et al.*, FEDERAL POWER COMMISSION, *Petitioners*,

v.

LO-VACA GATHERING COMPANY, HOUSTON PIPE LINE COMPANY, EL PASO NATURAL GAS COMPANY, *Respondents*.

On Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Fifth Circuit

JOINT BRIEF FOR RESPONDENTS IN OPPOSITION

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v.

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JOINT BRIEF FOR RESPONDENTS IN OPPOSITION

Come now Lo-Vaca Gathering Company (Lo-Vaca), Houston Pipe Line Company (Houston), and El Paso Natural Gas Company (El Paso), respondents herein, and file this joint brief in opposition to the petitions

for writ of certiorari filed by the People of State of California (California), *et al.*, No. 914, Southern California Gas Company (S. Cal. Gas), *et al.*, No. 915, and the Federal Power Commission (Commission), No. 990.

OPINIONS BELOW

The opinion of the Court of Appeals for the Fifth Circuit is reported at 323 F. 2d 190 (5th Cir. 1963). It is set forth in Appendix A to California's petition in No. 914. The order which denied petitions for rehearing and likewise denied the Commission's motion for rehearing *en banc* is contained in Appendix C to California's petition in No. 914. The opinion and orders of the Commission (R. 256-277, 332-334) are contained in Appendix A to the petition of S. Cal. Gas in No. 915.

JURISDICTION

The jurisdictional requisites are adequately set forth in the three petitions.

QUESTION

When a nonjurisdictional sale between two parties is separate from any jurisdictional sale between the same parties by reason of separate rates, separate negotiations, separate gas reserves, separate delivery points, separate metering, separate contracts, and separate regulatory control, is such sale converted into a jurisdictional sale when gas sold under such separate transaction is physically commingled by the purchaser with gas which is destined for resale subject to Commission jurisdiction?

STATUTE INVOLVED

The pertinent provisions of the Natural Gas Act (52 Stat. 821, 15 U.S.C. §§ 717-717w) are set forth in Appendix D to California's petition in No. 914.

STATEMENT

Respondents designed their physical operations so that their transactions would be entirely separate from any sales over which the Commission has jurisdiction. They also designed their operations so that their sales would not constitute sales in interstate commerce for resale subject to commission jurisdiction (R. 140-162, 343, 486-489, 494). Petitioners' statements provide selected factual details relating to Respondents' sales. But Petitioners seek to leave the incorrect impression that Respondents rely solely upon language in their restricted-use contracts to show that their sales do not lose their nonjurisdictional status because of commingling with other gas separately sold in interstate commerce for resale.

The record shows, as the court below found (323 F. 2d 190, 192, California Pet. App. A, p. 5), that Petitioners have carefully tailored their physical operations, as reflected by the language of their contracts, so that their restricted-use volumes would remain separately identifiable at all times (R. 140-162, 343, 486-487, 494). To illustrate these essential facts it is necessary to set forth a short additional statement.

These proceedings involve two types of sales. La Vaca proposes to make a direct sale of natural gas for El Paso's own use in facilities in New Mexico and Arizona (R. 820-846). Houston proposes to make a sale of gas to El Paso to be consumed wholly in Texas

in intrastate commerce (R. 416-458). Contrary to contentions of Petitioners (Cal. Pet. 16; S. Cal. Gas Pet. 10-11; E.P.C. Pet. 15), both sellers and the purchaser propose many physical operations which will ensure that gas sold under their restricted-use contracts will, at all times, be separately identifiable by volume (R. 160-162, 358, 486-489). This is not a case where jurisdiction is sought to be made dependent upon contract language alone.

Recitation of material facts demonstrates that the language of the restricted-use contracts of Lo-Vaca and Houston are but reflections of proposed operations of sellers and buyer which, in fact and in law, maintain separate identity of the restricted-use volumes at all times. The provisions in Respondents' restricted-use contracts commit the parties to conduct their entire operations in a prescribed manner in order that the restricted-use volumes will remain separately identifiable at every stage. Significantly, under the Federal Power Commission's regulatory procedures, all gas sold by El Paso at the California border is attributable to volumes sold under nonrestricted-use contracts which are subject to regulation by the Federal Power Commission; gas consumed at points of restricted use is attributable to volumes sold under restricted-use contracts which is subject to regulation by the State of Texas (see *infra*, pp. 21-22).

We turn first to Lo-Vaca which entered into two separate contracts with El Paso (R. 820-846, 847-873). Its restricted-use contract here is for the sale of 50,000 Mcf per day for El Paso's own use (R. 823, 825-828, 842). Its unrestricted-use contract, which is not involved here, calls for a sale of 70,000 Mcf per day (R. 850-851). Negotiations on the restricted-use con-

tract began in February, 1960, and culminated in execution of the contract on March 15, 1960 (R. 25, 281). Lo-Vaca will not produce any of the gas to be delivered to El Paso in satisfaction of this contract,[1] but has contracted with producers whose reserves will be separately dedicated to satisfaction of the restricted-use contract (R. 25-26, 875). These reserves are entirely separate from reserves to be used in satisfaction of Lo-Vaca's unrestricted-use contract (R. 64-65, 216).

Lo-Vaca will construct the necessary gathering facilities to deliver the gas to El Paso at the Coquat Station near Three Rivers, Texas (R. 33, 815, 819). At that location, the separate identity of the restricted-use volumes will be further preserved by separate metering at separate delivery points (R. 35, 257). Lo-Vaca has filed an application for a certificate authorizing the transportation to the Coquat Station (R. 812-817).

Houston also proposes a sale to El Paso at the Coquat Station of 50,000 Mcf per day for restricted use in Texas, either in El Paso's own facilities or for sale to Phillips Petroleum Company at its Goldsmith Gasoline Plant in Sutton County, Texas (R. 416-458). The source of this gas is separate from any other gas purchased by El Paso with separate metering at a separate delivery point (R. 266), and the volumes will, at all times, be separately identifiable (R. 141, 486, 487).

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[1] Thus, Petitioner, California, is mistaken when it contends that Respondents' rates to El Paso would have an adverse effect on the Commission's area price policy relating to producer sales (Cal. Pet. 12). The restricted-use sales by Lo-Vaca and Houston would not be producer transactions which alone are subject to the Commission's area price determinations. The producer sales to Lo-Vaca *would be* subject to Commission regulation.

It is also pertinent that Houston engages in an entirely intrastate operation along the Texas Gulf Coast (R. 104-106, 415). Its customers include many industrial concerns and city-gate customers. Importantly, many of the producers upon whom Houston is, in turn, dependent for its supply have provisions in their gas sales contracts permitting them to terminate before their gas may be resold in interstate commerce (R. 109-111, 459).[2] Therefore, if Houston is to maintain adequate service to its existing customers, it must be assured that none of its sales will be in interstate commerce (R. 179). Necessity for this assurance is underscored by the fact that Houston's entire system reserves guarantee performance of the El Paso restricted-use contract (R. 169, 173, 179-180).

El Paso, through its subsidiary, El Paso Gas Supply Company, will physically receive and transport Lo-Vaca's restricted-use volumes commingled with Houston's restricted-use gas and with other gas to be purchased under Lo-Vaca's unrestricted contract (R. 268-269, 486-487). However, the record shows that El Paso will maintain separate identification of restricted-use volumes not only through metering at all points of restricted use (R. 343, 486-487), but also through construction of substantial facilities at many points to assure that restricted-use gas can, at all times, be delivered and utilized at the points of restricted use (R. 145-160, 485, 489). These new facilities will include both minor installations at various points on El

[2] Such fact belies Petitioner's assertion that there is no business reason for Houston to desire to make a nonjurisdictional sale (See S. Cal. Gas Pet. p. 20). In any event, there is no requirement in the Act, or elsewhere, which makes it necessary to advance a business reason for not engaging in transactions subject to federal jurisdiction.

Paso's system and the laying of a major segment of pipeline consisting of 114 miles of 16 inch line from the Keystone Station to the El Paso Station (R. 140-145, 494). El Paso will operate its system so that the restricted-use volumes purchased from Lo-Vaca will never exceed the restricted use in El Paso's facilities in New Mexico and Arizona (R. 343, 486-487). In a like manner it will also operate its facilities in Texas so that its restricted-use purchases from Houston will never exceed consumption at the points of restricted use (R. 160-162, 358, 486-489).

From the foregoing facts, it is obvious that a continual separate identification of restricted-use volumes is maintained, not by contractual language alone, but by means of physical operations so that the transactions themselves are continually separate. *United States* v. *P.U.C. of California*, 345 U.S. 295, 317-318 (1953).

SUMMARY OF ARGUMENT

The rationale of the "separability test" which is determinative of the jurisdictional issue here has been described by the Commission, itself, in its brief in *North Dakota* v. *F.P.C.*, 247 F. 2d 173 (8th Cir. 1957) where it echoed this Court's reasoning in *United States* v. *P.U.C. of California*, 345 U.S. 295, 317-318 [Brief of Respondent, Federal Power Commission, No. 15669, United States Court of Appeals, Eighth Circuit, January 1957, p. 10]:

> "* * * For those decisions [*United States* v. *P.U.C. of California*, 345 U.S. 295 and *City of Hastings* v. *F.P.C.*, 221 F. 2d 31 (D.C. Cir. 1954)] make plain that the indistinguishable commingling of jurisdictional and non-jurisdictional gas in delivery is not sufficient in itself to require that

> sale of both be subjected to F.P.C. jurisdiction. In every case where there is commingling, indistinguishably, in a single flow, of some gas (or electricity) delivered in interstate commerce for resale, with other gas (or electricity) not delivered in interstate commerce, or not for resale, it is necessary for the Commission to determine 'whether [or not] an essentially separate transaction [for the nonjurisdictional delivery] . . . is identifiable' ".

Significantly, in *North Dakota*, the court applied the separability test in upholding commission denial of jurisdiction over restricted-use contracts (247 F. 2d 173, 177; see, *infra*, pp. 13-14).

The issue presented by Petitioners here is whether the decision below, which faithfully followed consistent court precedents in applying the separability test, should be overturned.

At the outset it is pertinent to note that the Commission has not only urged application of the established separability test in proceedings before this Court and lower courts,[3] but also has applied this test in numerous other cases which have come before it.[4]

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[3] See Brief of Respondent, Federal Power Commission, No. 11824, United States Court of Appeals for the District of Columbia Circuit, dated December 1953 and Brief of Federal Power Commission in Opposition, In the Supreme Court of the United States, No. 656, October Term, 1954 [both of the foregoing briefs relate to *City of Hastings* v. *F.P.C.*, 221 F. 2d 31 (D.C. Cir. 1954)]; Brief of Respondent, Federal Power Commission, No. 15669, United States Court of Appeals, Eighth Circuit, dated January 1957 [*North Dakota* v. *F.P.C.*, 247 F. 2d 173].

[4] See, *e.g.*, *Colorado Interstate Gas Co.*, 19 F.P.C. 1012 (1958); *Hope Producing Co.*, Docket No. G-15537, order issued February 3, 1959; *Shell Oil Co.*, 25 F.P.C. 1316, 1322 (1961); *City of Colton* v. *Southern California Edison Co.*, 26 F.P.C. 223 at 234-235, 237 (1961).

Notably, in a recent jurisdictional case involving the sale of electric energy the Commission expressly applied the separability test in holding a direct sale of energy for pumping purposes to be nonjurisdictional, despite commingling. *City of Colton* v. *Southern California Edison Co.*, 26 F.P.C. 223, 234-235 (1961)[5] (see, *infra*, pp. 27-28).

Furthermore, the Commission consistently applies the separability test in declaring that volumes transported by interstate pipelines for the account of ultimate consumers are not jurisdictional despite commingling with gas to be resold in interstate commerce (R. 1107). Indeed, it has issued certificates to major interstate pipelines whose economic feasibility has been dependent in large measure upon transportation of nonjurisdictional volumes commingled with resale volumes. See, *e.g.*, *Houston Texas Gas & Oil Corp., et al.*, 16 F.P.C. 118, 121-122 (1956); *Trans-Continental Gas Pipe Line Co., Inc.*, 7 F.P.C. 24, 29, 34 (1948) (see, *infra*, pp. 19-20).

This consistent court and commission interpretation repudiates Petitioners' contention that the lower court's decision constitutes a departure from established precedents or carves out an exception to Commission jurisdiction. On the contrary, the separability test applied by the lower court preserves the allocation of state and federal jurisdiction set forth in the Natural Gas Act (see, *infra*, pp. 16-19).

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[5] Affirmed, *sub nom.*, *F.P.C.* v. *Southern California Edison Co.*, No. 71, October Term, 1963, decided March 2, 1964, 84 S. Ct. 644. The Commission's denial of jurisdiction over the separate sale for pumping purposes, through application of the separability test, was not at issue on review.

Moreover, the separability test is both practical and realistic. It is practical, for as the lower court noted it avoids unnecessary expense of construction of separate facilities to transport the gas sold under non-jurisdictional transactions (323 F. 2d at 194). It is realistic, for the concept of separate identity by volume is not new but is practiced daily through commingling and proportional separation of fungible commodities in such businesses as grain elevators and pipe lines (*Ibid.*). See *Federal Tender Board No. 1* v. *Haynes Oil Corp.*, 80 F. 2d 468 (5th Cir. 1935).

We analyze below applicable cases which have consistently and correctly applied the separability test in factual situations indistinguishable in principle from the Lo-Vaca and Houston restricted-use sales (*infra*, pp. 10-16). We consider also Petitioners' contention that the lower court's decision would result in a gap in regulation (*infra*, pp. 16-23). Finally, we review briefly other jurisdictional cases, not involving the separability test, which are cited by Petitioners in their effort to expand Commission jurisdiction beyond the limited delegation of Section 1(b) of the Natural Gas Act (*infra*, pp. 24-28).

ARGUMENT

I

The Decision Below Is Clearly Correct

In holding that the restricted-use sales proposed by Lo-Vaca and Houston are not subject to federal jurisdiction, the court below followed an unbroken line of cases to reach the demonstrably correct result. *U.S.* v. *P.U.C. of California*, 345 U.S. 295 (1953); *City of Hastings* v. *F.P.C.*, 221 F. 2d 31 (D.C. Cir. 1954); and *North Dakota* v. *F.P.C.*, 247 F. 2d 173 (8th Cir. 1957). By attacking the lower court's decision Petitioners

would overturn the rationale of this Court in *California.*

Petitioners contend that Lo-Vaca's sale to El Paso for its own use in Arizona and New Mexico and Houston's sale to El Paso for consumption entirely in Texas are converted into sales for resale in interstate commerce because the restricted-use volumes would be commingled with gas destined for resale at the California border (Cal. Pet. 11, S. Cal. Gas Pet. 6-14, F.P.C. Pet. 10-11). Although they cannot deny that El Paso will always operate its system so that it will consume, at the restricted-use points, volumes equal to or greater than the restricted-use volumes to be purchased from Lo-Vaca and Houston (R. 145-162, 485), and that such system operation will faithfully maintain separate identification of restricted-use volumes (R. 141, 160-162, 343, 358, 486-489), they urge the Court to ignore these facts and hold that commingling alone converts these separate transactions into sales for resale in interstate commerce.

But, as the lower court recognized, the law is to the contrary. In *California*, this Court was presented with facts which showed that the energy sold to the Navy in California for its own use in Nevada was sold under the same contract as energy sold to the Navy for resale in interstate commerce: There was *one* delivery point, *one* sale, and *no* separate metering. This Court overturned attempted regulation of the sale by the State of California, holding that Federal Power Commission jurisdiction over the energy sold for resale necessarily extended to all energy sold under the *single* contract (345 U.S. at 317-318). In doing so, the Court expressly approved the separability test declaring that if there had been evidence of "separate rates, separate negoti-

ations, separate contracts, or separate rate regulation by official bodies, in short that the 'sales' themselves were separate", the opposite result would have been reached" (*ibid.*).

Likewise, *Hastings*, was properly relied upon by the lower court for it illustrates the applicability of the separability test to the facts of the Lo-Vaca sale. There, Kansas-Nebraska Natural Gas Company made a direct sale in interstate commerce to the City of Hastings for use in an electric generating plant. Under a separate contract, Kansas-Nebraska made a sale to the City for resale to ultimate consumers. All volumes were delivered at the city gate in a commingled stream. The City transported the volumes, still commingled, to the points of use.

Thus, contrary to the Commission's implication here (F.P.C. Pet. 17), it was simply not possible to determine whether the actual molecules of gas delivered at the city gate under the contract restricting use to consumption at the generating plant were, in fact, used for that purpose. As a matter of physical fact, molecules of gas sold to the City under the restricted-use contract were necessarily resold to ultimate consumers without converting the restricted-use sale into a sale for resale. The inescapable fact is that, where all elements of separability are present, molecular tracing is not determinative. In a close parallel to Petitioners' contention with regard to Lo-Vaca's sale, some *molecules* of the restricted-use gas in *Hastings* would be resold, but the restricted-use *volumes* of the fungible commodity were always identifiable.

Notably, in *Hastings* the Commission filed with this Court a brief in opposition to the granting of a writ

of *certiorari* arguing that the separability test enunciated by this Court in *California* was controlling and that there existed "no conflict of decisions and no need for further review" (Brief of Federal Power Commission in Opposition, In the Supreme Court of the United States, No. 656, October Term, 1954, pp. 13, 18). This Court denied *certiorari* [349 U.S. 920 (1955)].

Similarly, *North Dakota* presents facts substantially the same as those presented by Houston's sale. Gas was sold by Signal Oil and Gas Company and Amerada Petroleum Corporation at the outlet of a gasoline plant in North Dakota to Montana-Dakota Utilities Company. Four contracts were involved. Each producer entered into an interstate resale contract and an intrastate resale contract. All gas for all four sales was commingled in Montana-Dakota's line. Before the commingled stream left the State of North Dakota, some volumes were metered off to four communities in satisfaction of the two intrastate, nonjurisdictional contracts.

The court affirmed the Commission's denial of jurisdiction over the restricted-use volumes, holding (247 F. 2d 173, 177):

> "We think, then, the gas sold pursuant to such 'firm gas' contracts for consumption in North Dakota is clearly distinguishable from the 'dump gas' sold in interstate commerce. There is no commingling of interstate with intrastate gas within the State of North Dakota in the sense of loss of identity because the intrastate gas going to the four North Dakota communities named is separated from the gas stream in the main line and metered before any portion of the gas stream has left the State of North Dakota. Accordingly, the

> quantities of intrastate gas purchased by Montana-Dakota under the 'firm gas' contracts are easily identifiable and determinable."

But the Commission contends that *California*, *Hastings*, and *North Dakota* are distinguishable because each involves only a single source of supply for the restricted use, whereas here gas consumed at the points of restricted use could physically be derived from many sources (F.P.C. Pet. 17). Curiously, the Commission argues that molecular identification is prerequisite to determination of no jurisdiction if gas from several sources is involved, but if gas from only one physical source is sold under several contracts molecular tracing is not necessary (F.P.C. Pet. 17).

But obviously the number of sellers or sources of gas is irrelevant, for in each of the decided cases the *molecules* of gas sold under the restricted-use contracts were not identifiable, because of commingling, and might be resold. The critical fact in each case, as here, is that the *volumes* of gas sold under the restricted-use contracts remain separately identifiable. The manifest irrelevance of the Commission's distinction doubtless accounts for the significant fact that it played no part in the rationale of any one of the three court opinions or in the Commission's own decisions from which Petitioners now seek to escape.

It is simply irrelevant whether gas for the restricted use may be attributable to only one seller, if that seller supplies both restricted-use and nonrestricted-use gas which is commingled in the buyer's pipeline. For example, in *Hastings*, some molecules of the gas delivered to the City at the city gate under the nonjurisdictional contract clearly would, because of commingling, be resold by the City, and, correspondingly, some of the gas

sold under the nonrestricted-use contract would be consumed at the generating plant. It is equally clear that some molecules of the restricted-use gas supplied in *North Dakota* would, because of commingling, be resold in interstate commerce.

Furthermore, the Commission's suggested importance of a single source is at odds with the facts in *North Dakota*, for there were *two* sellers, in that case, not just one. Gas was sold under four contracts. The record in *North Dakota* shows that Signal contributed 15% of the total volumes of gas to the commingled stream. The combined total volume delivered annually into the commingled stream was approximately 6,867,270 Mcf. Of this amount, Signal delivered only about 1668 Mcf under its restricted-use contract. Undeniably, it would be impossible to trace the commingled molecules of gas from the point of entrance into Montana-Dakota's line to the point of consumption. Molecules delivered to the points of restricted use could come from the 1,028,423 Mcf delivered under Signal's unrestricted-use contract or from the 5,827,727 Mcf delivered under Amerada Petroleum Corporation's unrestricted contract, or even from the 9,452 Mcf delivered to Montana-Dakota under Amerada's restricted-use contract.[6] Conversely, molecules of the restricted-use gas could and did flow into interstate commerce for resale.

The number of sellers or sources of gas has no relevance to jurisdiction. The Commission's argument leads to the absured conclusion that a sale which is non-

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[6] The Examiner's decision in *North Dakota* contains findings from which the data referred to above is derived. See *Montana-Dakota Utilities Co.*, 16 F.P.C. 401, 405 (1956).

jurisdictional when begun may suddenly be converted into a jurisdictional sale through no action on the part of seller or change in operations of the buyer other than the purchase of additional supplies of gas.

Clearly, the lower court was correct when it adhered to the rationale of the separability test as enunciated in *California* and applied in *Hastings* and *North Dakota*.

II.

Decision Below Preserves the Congressional Division of Jurisdiction Provided in the Natural Gas Act

It is beyond dispute that, in the absence of commingling, Lo-Vaca's restricted-use sale would be a nonjurisdictional sale in interstate commerce for El Paso's own use. Correspondingly, Houston's sale would be a nonjurisdictional sale in intrastate commerce. As the court below noted, if the restricted-use volumes were physically segregated, the Commission would not claim jurisdiction over the sales (323 F. 2d at 191, California Pet. App. A, p. 3). But California claims the decision below would open a "regulatory gap" (California Pet. 13-15). The Commission, though urging the existence of a "gap" in regulation (F.P.C. Pet. 18) is careful to couch its allegation in terms, not of lack of power of the State of Texas to regulate the sales, but in terms of what it believes to be a disinclination on the part of Texas to exercise an admitted power (F.P.C. Pet. 18). The Commission's tacit admission of state power is significant, for jurisdiction under the Act is based upon the nature of the transaction, not the manner in which the state or federal

government chooses to utilize its power.[7] *F.P.C.* v. *Southern California Edison Co.*, No. 71, October Term, 1963, decided March 2, 1964, 84 S. Ct. 644, 649-650.

The arguments urged by Petitioners in order to raise a spectre of a regulatory gap would blur the "bright line" drawn between federal and state jurisdiction in the Natural Gas Act. *F.P.C.* v. *Southern California Edison Co.*, 84 S. Ct. at 651, *Panhandle Eastern Pipe Line Co.* v. *P.S.C. of Indiana*, 332 U.S. 507, 516-517 (1947). Petitioners overlook the division of jurisdiction and the limited delegation of Commission power which was reviewed in detail in *Panhandle* when this Court concluded (332 U.S. at 516-517):

> "Three things and three only Congress drew within its own regulatory power, delegated by the Act to its agent, the Federal Power Commission. These were: (1) the transportation of natural gas in interstate commerce; (2) its sale in interstate commerce for resale; and (3) natural gas companies engaged in such transportation or sale."
>
> * * * * *
>
> "Direct sales for consumptive use of whatever sort were excluded.
>
> "The line of the statute was thus clear and complete. It cut sharply and cleanly between sales for resale and direct sales for consumptive uses. No exceptions were made in either category for particular uses, quantities or otherwise. And the

[7] Obviously, for example, prior to this Court's decision in *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672 (1954) the fact that the Commission did not choose to exercise jurisdiction over producer sales for resale in interstate commerce did not mean that the Commission lacked jurisdiction. Similarly, the manner of state regulation is not determinative of its jurisdiction, or conversely of federal jurisdiction delegated by the Natural Gas Act.

> line drawn was that one at which the decisions had arrived in distributing regulatory power before the Act was passed.[12]" (Footnote omitted)

Clearly, since passage of the Natural Gas Act there has been, and can be, no regulatory gap (*id.*, at 517-520). Such a gap existed before enactment because states were powerless to regulate sales for resale in interstate commerce. *Missouri* v. *Kansas Natural Gas Co.*, 265 U.S. 298 (1924); *P.U.C. of Rhode Island* v. *Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927). But, states have always had the power to regulate direct sales in interstate commerce taking place within their borders and all sales in intrastate commerce. *P.U.C. of Kansas* v. *Landon*, 249 U.S. 236 (1919); *Pennsylvania Gas Co.* v. *P.S.C. of New York*, 252 U.S. 23 (1920); *Panhandle Eastern Pipe Line Co.* v. *P.S.C. of Indiana*, 332 U.S. 507 (1947). The purpose of the Natural Gas Act was to authorize the Federal Government, through the Commission, to regulate only in that area of interstate commerce where states are powerless to act; namely, sales for resale in interstate commerce (332 U.S. at 516). Hence, the language of the Natural Gas Act is explicit and restrictive in its delegation that [15 U.S.C. § 717(b)]:

> "The provisions of the act shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale . . . but shall not apply to any other transportation or sale of natural gas . . ."

The comprehensive regulatory scheme prescribed by by the Act and noted by this Court in *Panhandle* (332 U.S. at 520) and in *Southern California Edison*, 84 S. Ct. at 649-651, of course, does not provide the Commission with power over transactions which do not come

within its limited delegation of authority. As this Court held, the Act does not give power over any direct sales in interstate commerce of "whatever sort" or over sales in intrastate commerce (332 U.S. at 517).

This obvious fact was also recognized by this Court, in *F.P.C.* v. *Transcontinental Gas Pipe Line Corp.*, 365 U.S. 1, 17 (1960), which involved producer sales made in interstate commerce directly to the consumer. After the sale, the restricted-use gas was commingled in a transporter's pipeline with other gas to be sold for resale in interstate commerce. Significantly, so far as the Commission's novel single-source distinction is concerned (*supra*, pp. 14-15), gas in Transcontinental's commingled stream came from many sources, not just one. But this Court agreed that the Commission had no jurisdiction over the producers' direct sales even though the gas was physically commingled with other volumes in the interstate line so that the molecules could not be traced to the point of restricted use (*id.*, at 4).

It is significant, in light of the Commission's attack here upon the separability test, that direct sale-transportation arrangements like the one in *Transcontinental* are common in the industry. Customarily, such an arrangement involves a direct sale by the producer in or near the field to an ultimate consumer, such as a power company, which uses the gas in generation of electric energy. Thus, as in the Lo-Vaca restricted-use sale, the producer may make a sale in Texas for consumption in another state. *Cf.*, *Houston Texas Gas & Oil Corp., et al.*, 16 F.P.C. 118 (1956), affirmed *sub nom.*, *Florida Economic Advisory Council* v. *F.P.C.*, 251 F. 2d 643 (D.C. Cir. 1957) *cert.* denied, 356 U.S. 959 (1958). After the direct sale to the con-

summer, the gas is physically commingled in an interstate pipeline with other gas to be resold.

The direct sale is not subject to Commission jurisdiction, as held in *Transcontinental*. Yet, the arguments newly urged by the Commission in its attempt here to assert jurisdiction over the Lo-Vaca and Houston sales would be equally applicable to the direct sale-transportation arrangements. Since there is no regulatory gap with respect to the direct sale in Texas for power-plant consumption in New York or Florida, by the same token there can be no regulatory gap with respect to a direct sale in Texas for El Paso's consumption in New Mexico and Arizona. The "regulatory gap" argument is obviously spurious.

The direct sale-transportation arrangements also serve to illustrate the general industry practice, accepted by the Commisison, to treat gas as a fungible commodity. Indeed, the Commission bases the exercise of its certification power in cases of major national importance upon express recognition of the fungibility concept. For example, in the *Houston Texas Gas & Oil* case, *supra*, the Commission authorized construction of a new pipeline system extending from southern Texas to Florida. Of a total initial system capacity of 250,000 Mcf per day, 150,000 Mcf or three-fifths, was dedicated to transportation of gas purchased in Texas by electric generating companies in Florida. The remaining 40% of the capacity was dedicated to resale gas (16 F.P.C. at 121-122). The pipeline is dependent for its existence upon the nonjurisdictional sales to the power companies.[8]

[8] Another example of Commission certification of a major interstate pipeline company which was dependent in significant part upon transportation volumes is *Trans-Continental Gas Pipe Line Corp., Inc.*, 7 F.P.C. 24, 29, 34 (1948).

Plainly, the comprehensive scheme envisioned by the Act, followed by the Commission until this proceeding, and still followed in cases of major national importance involving direct sale-transportation arrangements, is preserved, not disrupted, by the lower court's decision. It is the Commission, through its inconsistent refusal to apply the separability test, which would disrupt the comprehensive scheme of federal and state regulation provided by the Act.

Furthermore, it simply is not accurate for the Commission to suggest that the State of Texas has no interest in regulation of transactions within its jurisdiction (F.P.C. Pet. 18). The Commission, itself, has recently found that, with regard to Lo-Vaca's existing operations (*United Gas Pipe Line Co.* v. *Coastal States Gas Producing Co.*, Docket No. CP64-75, Opinion No. 419, issued February 10, 1964, mimeo. ed., p. 4):

> "* * * [A] certificate of the Texas Railroad Commission has been filed with us in accordance with the provisions of Section 1(c) of the Act to the effect that the rates, services, and facilities of Lo-Vaca involved in its sales of natural gas for resale in Texas are subject to its [The Texas Railroad Commission's] regulatory jurisdiction and it is exercising such jurisdiction."

Patently, the State of Texas does have an interest in regulation of transactions falling within reach of its authority. Also, with regard to the power of the State of Texas to regulate sales, it is pertinent to note that city gate rates are fixed by the Texas Railroad Commission. *State of Texas* v. *Public Service Corporation of Texas*, 88 S.W. 2d 627 (1955), Tex. Civ. App. error refused; *Railroad Commission* v. *Houston Natural Gas Corp.*, 289 S.W. 2d 559 (1956). And under applicable

Texas law, the Railroad Commission has equally broad power to regulate industrial sales. *United Gas Corp. v. Shepherd Laundries Co.*, 189 S.W. 2d 485 (1945).

Nor may it be suggested that the Commission's power over activties within its delegated authority is in any way diminished by its lack of authority over the Lo-Vaca and Houston restricted-use sales. The Commission admits that commingling does not convert direct sale-transportation agreements into jurisdictional sales (R. 1107) and that commingling does not affect the jurisdictional status of restricted-use sales where all gas comes from one source (F.P.C. Pet. 11). Therefore, there is no basis for a contention that Commission jurisdiction over the Lo-Vaca and Houston sales is essential to maintain regulation over all commingled volumes in El Paso's system.

In this regard, also, it should be noted that the concern of California and S. Cal. Gas that gas sold for resale at the California border will be unregulated is groundless. The Commission will continue to regulate El Paso's sales for resale at the California border. And, pursuant to standard regulatory procedure used to allocate jurisdictional and nonjurisdictional costs, the gas resold at the California border will be attributed to gas purchased by El Paso under jurisdictional sales, not Lo-Vaca and Houston restricted-use sales.

Moreover, a review of the entire operations involving the Lo-Vaca and Houston restricted-use gas demonstrates that the Commission's power within its specifically delegated sphere remains plenary. Thus, the gas sold to Lo-Vaca for its restricted-use sale will come from separately dedicated reserves sold under producer contracts (R. 25-26, 875). These producer sales will be sales for resale in interstate commerce

and hence subject to Commission regulation. Significantly, the Commission's area price policy relating to producer sales for resale in interstate commerce will be applicable to these sales to Lo-Vaca.

Lo-Vaca will gather and transport this restricted-use gas from points of production to the Coquat Station. This delivery by Lo-Vaca will be subject to the Commission's certification power over transportation of natural gas in interstate commerce [Section 1(b), 15 U.S.C., § 717(b)]. Of course, Lo-Vaca filed an application for a certifiate authorizing such transportation (R. 812-817). The transportation of Lo-Vaca's restricted-use gas in El Paso's system will likewise be transportation in interstate commerce regulable by the Commission, and El Paso must obtain a certificate therefor. But *Transcontinental* shows that such authority does not extend to direct sales in interstate commerce, nor does it extend to the intrastate activities of Houston or El Paso.[9] (365 U.S. at 17)

In this context, the lower court aptly concluded (323 F. 2d at 194-195):

> "* * * The method of segregation used here seems to be the most practical one. No one has suggested to us any reason why the mixing or commingling of this gas with other gas hampers the regulation of sale of the 'jurisdictional' gas, or in any manner tends to subvert the national policy. No one has suggested that petitioners will not carefully and conscientiously carry out the terms of their contracts. In short, we can find no prejudice to anyone's legitimate interests in the consumation of these plans."

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[9] It is established beyond all question that a company may participate in jurisdictional and nonjurisdictional activities by use of the same facilities. *Colorado Interstate Gas Co. v. F.P.C.*, 324 U.S. 581, 585-586 (1945).

III.

The Decision Below Does Not Conflict With Any Decision of This Court or of Any Other Court

Cases involving the separability test when applied to commingled volumes are relatively few, perhaps bespeaking the relative infrequency of this type of transaction. As demonstrated above, (*supra*, 10-16) the lower court correctly analyzed the applicable cases in reaching its conclusion. The lower court was also correct in rejecting the contention urged upon it by Petitioners that this case is controlled by decisions such as *Deep South Oil Co.* v. *F.P.C.*, 247 F. 2d 882 (5th Cir. 1957), or *Pennsylvania Water & Power Co.* v. *F.P.C.*, 343 U.S. 414 (1952), which did not involve the separability test at all.

In *Deep South*, gas for intrastate use and for resale in interstate commerce was sold under one contract. The court rejected contentions that an admitted sale for resale in interstate commerce was excluded from Commission jurisdiction either on the ground that it took place during production and gathering, or because it involved the sale of casinghead gas for extraction of heavy hydrocarbons, or because it was not a sale of natural gas (247 F. 2d 887-889). *Deep South* did not involve the separability test. It dealt with the scope of exemptions from the primary grant of jurisdiction in Section 1(b) over sales for resale in interstate commerce. But that question is not here. The question here is whether the Lo-Vaca and Houston sales fall within the primary grant, *i.e.*, whether they are sales for resale in interstate commerce.

Petitioners' reliance upon language of the opinion in *Connecticut Light & Power Co.* v. *F.P.C.*, 324 U.S. 515, 529 (1945) is likewise misplaced. They suggest that the holding in *Connecticut* was that "Federal

jurisdiction was to follow the flow of electric energy, an engineering and scientific test, rather than a legalistic or governmental test." But, this is not the Court's holding. That quoted language merely explained the scope of the bill as originally drafted (324 U.S. at 529-530). Indeed, the Court noted that such a test would extend jurisdiction to the toaster on the breakfast table. But when the bill was enacted, jurisdiction was limited by Congress to cover only those transactions not regulable by the states. Therefore, legal concepts, such as "sales for resale," "direct sales," and "local distribution" were utilized in prescribing and proscribing Commission jurisdiction.

By the same token, cases cited by the Commission (F.P.C. Pet. 14) dealing with the scope of constitutional authority of the Federal Government over interstate commerce have no application here. None involve the limited delegation of Section 1(b) of the Act. None involve the separability test.

Neither are the holdings in *Pennsylvania Water & Power Co.* v. *F.P.C.*, 343 U.S. 414 (1952) or *F.P.C.* v. *Southern California Edison Co.*, 84 S.Ct. 644, controlling here. In *Penn Water* the question presented was whether a sale for resale escaped federal jurisdiction because a large proportion of the energy resold was produced in the state of consumption. The Court held that the sale of all of the energy under *one* contract was jurisdictional because it included some energy from out of state. Admittedly, the Commission had jurisdiction over the sale of the out-of-state energy, and since all energy was sold in a *single* sale under a *single* contract, Commission regulation of the out-of-state energy necessarily extended to all energy sold. (343 U.S. at 419-420). This Court distinguished the *Penn Water* holding in *California* where it stated (345 U.S. at 317):

> "* * * We held there [in *Penn Water*] that the federal rate authority must apply to all electricity sold, despite the fact that it was made up of power transmitted across state lines as well as that produced locally. The impossibility of separating interstate from intrastate electricity consumed by each purchaser is patent. In such a case, federal rate jurisdiction must attach to each distributor's negotiated agreement with the seller irrespective of occasional and unpredictable use of nonjurisdictional intrastate power.
>
> "There, however, the problem was whether the sales of electricity were in 'interstate commerce'. Here, it is a different one whether the entire sale is a 'sale for resale.'"

This Court then continued to announce the separability test (*supra*, pp. 7-8).

Similarly, in *Southern California Edison*, this Court's holding did not reach the question here. That case decided that when energy is sold for resale under one contract which includes out-of-state energy, such sale is a sale in interstate commerce subject to Commission regulation. Commission jurisdiction attaches in such instances, the Court held, even though the energy would be consumed within the state of sale and regardless of Commission regulation of preceding transactions involving the same energy on its journey from the point of production to the point of consumption. In essence, the *Southern California Edison* case holds that there is no exemption under Section 201(b) of the Federal Power Act analogous to the Section 1(c) amendment to the Natural Gas Act.[19]

[19] Section 1(c) of the Natural Gas Act declares that sales for resale of gas received within the boundary of a state are matters of local, not national concern, if *all* such gas is ultimately consumed within such state. 15 U.S.C. § 717(c). See Appendix D to California Petition.

It is significant in the context of the Commission's argument against the separability test here to note that the Commission itself utilized the separability test in the *Southern California Edison* case when that proceeding was before it *concurrently with the Lo-Vaca and Houston proposals.* The Commission held, in circumstances remarkably analogous to the Lo-Vaca facts, that a direct sale in interstate commerce for pumping purposes was not converted into a jurisdictional transaction because of commingling. The Commission's rationale is particularly pertinent here for it held [26 F.P.C. 223, 235 (1961)]:

> "In the present case we have concluded that Edison's presently effective rate is embodied in its 1945 contract. The rate set forth in the contract is composed of a demand charge and an energy charge applicable both to the delivery for resale and the deliveries for pumping purposes, but these deliveries were metered separately. In its order of August 17, 1954, the PUC, in addition to prescribing separate rate schedules for the deliveries for resale at the City of Colton Substation on the one hand, and the deliveries for pumping purposes on the other, permitted separate metering and billing for the pumping sales, and this *separate metering* and *billing* commenced September 13, 1954, and has continued since that time.
>
> "Thus a *separation* of the *pumping deliveries from the deliveries for resale has plainly been achieved.* Irrespective of the invalidity of the PUC's orders, a *separation in fact* is not only feasible but *has been accomplished.* Under *United States* v. *Public Utility Comm'n., California Electric Power Co.* v. *F.P.C.* and *City of Hastings* v. *F.P.C., supra*, there is no justification for our asserting jurisdiction in such a case over the separated non-jurisdictional transaction. We fur-

> ther find that if the question of separation had been properly presented by appropriate filings in 1954, the same conclusion should have been reached. We conclude that the *public interest* will be served by treating the deliveries for pumping purposes alone as having been separate sales since September 13, 1954, and by treating only the sale for resale as subject to our jurisdiction." [Emphasis supplied].

Clearly, since it was in the public interest to "treat", through use of the separability test, a sale of electric energy for pumping purposes as nonjurisdictional,[11] it is likewise in the public interest to "treat", through use of the same criteria, a sale of gas for compressor fuel as nonjurisdictional.

From the foregoing, it is apparent that the petitions herein, do not present a case of first impression. This Court, lower courts, and the Commission, itself, have all applied the separability test consistently in determining the jurisdictional status of transactions. The Commission's attempt here to expand its jurisdiction to cover the Lo-Vaca and Houston restricted-use sales simply because of commingling of gas in El Paso's line constitutes a radical departure from these precedents. As recognized by the court below, such an extension of jurisdiction would require modification of Section 1(b) of the Act which can be accomplished only by Congress (323 F. 2d at 194).

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[11] Contrast this Commission holding giving viability to the separability test in a sale of electric energy with its counsel's attack on the separability test (F.P.C. Pet. 19, note 16) on the ground that such test might be applied to a sale of electric energy.

CONCLUSION

For all the foregoing reasons, Respondents submit that the lower court correctly interpreted the scope of Commission jurisdiction under Section 1(b) and correctly applied applicable court precedents. The lower court's decision does not create any gap in regulation but preserves the regulatory scheme set forth in the Act as construed by this Court. Moreover, the decision recognizes the practical nature of natural gas as a fungible commodity while maintaining the integrity of Commission regulation within its delgated authority.

Accordingly, Respondents urge that the petitions for writs of *certiorari* in Nos. 914, 915, and 990 be denied.

Respectfully submitted,

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